Important Tax Information About TSP In-Service Withdrawal Payments

Amounts paid to you from your Thrift Savings Plan (TSP) account are taxable income to you for Federal income tax purposes in the year in which payment is made. This notice summarizes the tax rules that apply to TSP in-service withdrawals, i.e., age-based (age 59½ or older) and financial hardship withdrawals. To see how this applies to your TSP payment, **read this notice carefully.**

We are required by law to provide you with this notice; however, because tax rules are complex, you may wish to consult a tax advisor before you make any decision.

1. Tax Withholding

Age-Based Withdrawals

Age-based in-service withdrawals are the only TSP payments made to participants before they separate from Federal service which are considered **eligible rollover distributions**, and the following Federal income tax withholding rules apply. (The TSP does not withhold amounts for state or local income tax.)

- The mandatory tax withholding on all eligible rollover distributions of $200 or more paid in a single year is 20%. The 20% is tax withholding, not actual tax due; therefore, when you file your annual Federal income tax return, you may be entitled to a refund of a portion of this amount, or you may be required to pay an additional amount.
- You can avoid withholding on all or any portion of your eligible rollover distribution by asking the TSP to transfer that amount to an IRA (other than a "Roth" IRA) or other eligible retirement plan.[1] However, you **cannot** avoid the mandatory 20% withholding on any amount that you elect to receive directly, even if you then roll it over to an IRA or other eligible retirement plan. (*See Section 2 of this notice.*)
- You may elect to have an amount withheld in addition to the 20% withholding by completing Line 3 of IRS Form W-4P, Withholding Certificate for Pension or Annuity Payments, and submitting it to the TSP Service Office along with your in-service withdrawal request. Line 1 and Line 2 are not valid elections for this type of payment.

Financial Hardship Withdrawals

A financial hardship in-service withdrawal is a **non-periodic payment** and cannot be transferred or rolled over to an IRA or other eligible retirement plan. The TSP will withhold 10% for Federal income tax from these payments unless the TSP Service Office receives from you IRS Form W-4P, Withholding Certificate for Pension or Annuity Payments. If you submit Form W-4P, you may elect:

- to have no Federal income tax withheld, by completing Line 1 of Form W-4P; or
- to have an amount withheld in addition to the 10% by completing Line 3 of Form W-4P.

Note: Line 2 is not a valid election for this type of distribution.

2. Transferring or Rolling Over Your Age-Based In-Service Withdrawal

All or any part of your age-based in-service withdrawal can either be transferred or rolled over to an IRA (other than a "Roth" IRA) or other eligible retirement plan. This permits you to postpone paying tax on that amount until you withdraw the money from the IRA or plan.

A **transfer** occurs when you instruct the TSP to send all or part of your distribution directly to an IRA or other eligible retirement plan instead of issuing it to you. Mandatory 20% Federal income tax withholding does not apply to an amount that the TSP transfers directly to an IRA or other eligible retirement plan; **however, it does apply to any payment made to you, even if you then roll it over.**

A **rollover** occurs when the TSP makes a distribution to you (which includes the amount of the payment you receive plus the amount of tax withheld) and you deposit any part of that distribution into an IRA or other eligible retirement plan within 60 days of the date you receive it.

In deciding whether to choose a transfer or a rollover, you should consider the following:

- You must pay Federal income tax on any part of the payment that you do not transfer or roll over. (*See Section 4 of this notice.*)
- Because all eligible rollover distributions of $200 or more made directly to you are subject to mandatory 20% withholding, you must pay Federal income tax on the amount withheld for taxes — even if you roll over the amount you receive — unless you deposit personal funds into your IRA or other plan equal to the amount withheld. (If you do this,

[1] An "eligible retirement plan" is defined in section 402(c)(8) of the Internal Revenue Code. Generally, an eligible retirement plan is an Individual Retirement Account (IRA) or an individual retirement annuity (other than an endowment contract); a qualified pension, profit-sharing, or stock bonus plan; or an annuity plan described in section 403(a) of the Internal Revenue Code. The IRA or plan to which your account is transferred must be a trust established inside the United States (i.e., the 50 States and the District of Columbia).

you may receive a refund of taxes withheld, but you cannot wait until you receive a refund of the withheld amount to complete a rollover.)

Therefore, if you do not want to use personal funds to make up the amount withheld, you should choose to have the TSP transfer your account to your IRA or other plan directly, instead of rolling it over to your IRA or other plan yourself.

Whether you choose a transfer or a rollover, the following rules apply:

You may transfer or roll over your payment into any IRA (other than a "Roth" IRA). However, if you want to roll it into the qualified plan of another employer at a later date, you should instruct the financial institution to establish a "conduit" IRA for you. Such an account can only contain amounts that are transferred or rolled over from a qualified plan; it cannot contain other contributions (whether deductible or nondeductible). IRAs containing other contributions cannot be rolled over into a plan maintained by another employer.

3. Tax Reporting

The TSP will report to the IRS all payments that are made directly to you as well as all transfers made to IRAs or other eligible retirement plans. We will also report TSP payments and transfers to the state in which your TSP account record shows you resided at the time payment was made, if that state has an income tax.

In January of the year that follows your payment, the TSP will send you IRS Form 1099-R, Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc. **Be sure your agency keeps your TSP account address up to date so that you receive the form and other important information about your account.**

You should include the amount reported on Form 1099-R as income on your individual income tax return for the year in which payment was made. However, you should then exclude from the adjusted gross income on your return any amounts that were transferred or rolled over. Attach a copy of Form 1099-R to your Federal tax return.

4. Early Withdrawal Penalty Tax

Under the Internal Revenue Code, an early withdrawal penalty tax of 10% is imposed on the total amount of an in-service withdrawal payment that you receive directly from the TSP (including any tax withholding) **before you become age 59½.** Thus, if you request a financial hardship withdrawal and are younger than age 59½, the penalty tax will apply to you. The penalty tax is in addition to the ordinary income tax that you pay on TSP payments.

The early withdrawal penalty tax does not apply if you are age 59½ or older. It also does not apply to TSP distributions used for the payment of medical expenses which would be deductible under the Internal Revenue Code. (*See IRS Form 5329, Additional Taxes Attributable to IRAs, Other Qualified Retirement Plans, Annuities, Modified Endowment Contracts, and MSAs.*)

5. Ten-Year Tax Option

If the payment you receive from the TSP qualifies as an **eligible lump sum distribution**, you may be able to lower the income tax you pay by using the **10-year tax option**.

An **eligible lump sum distribution** is one in which your total TSP account balance is distributed to you within one tax year (the calendar year for most taxpayers), regardless of whether this occurs in one or more payments. With the **10-year tax option**, your eligible lump sum distribution is taxed as if it were paid to you over 10 tax years.

The following rules apply to the 10-year tax option:

- The 10-year tax option is available only if you were age 50 before January 1, 1986.
- You must have been an **active participant** in the TSP for at least five years before the year in which your distribution is made. You are considered an active participant during a year if a contribution was made to your TSP account by either you or your agency during that year.
- You must use the 10-year tax option for all eligible lump sum distributions that you receive in the same tax year. This includes a withdrawal of your entire TSP account after separation and any taxable loan distribution. It also includes an eligible lump sum distribution from any other plan maintained by another employer (but excludes such distributions from IRAs).
- You can use the 10-year tax option only once in your lifetime. This means that if you use it in one tax year (e.g., for an age-based in-service withdrawal of your entire TSP account balance), you cannot use it for a distribution received from the TSP or another plan in any subsequent year.
- You must use the tax rates in effect in 1986.
- If you transfer or roll over all or any part of your distribution, you cannot use the 10-year tax option.

You can elect the 10-year tax option by filing IRS Form 4972, Tax on Lump Sum Distributions, with your annual income tax return.

6. TSP Service Office Information

If you have any questions regarding this notice, please contact the TSP Service Office at (504) 255-6000 (TDD: (504) 255-5113) or write to:

TSP Service Office
National Finance Center
P.O. Box 61500
New Orleans, LA 70161-1500